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7500 Flying Cloud Drive, Suite 900 · Eden Prairie, MN 55344
Phone: +1 952 253.6231 · Fax: 952 835 4774

www.midwestshippers.com

Statement of the Midwest Shippers Association

Bruce Abbe, Executive Director

To the Public Hearing of the United States Surface Transportation Board

To Review the Current STB Commodity, Boxcar and

TOFC/COFC Intermodal Container Rail Shipping Regulatory Exemptions

Docket No. EP 704

January 31, 2011

On behalf of the board of directors and members of the Midwest Shippers Association we want to commend the Surface Transportation Board for holding this important public hearing to review the "Exemptions" categories of rail traffic that currently are exempt from federal regulation.

We at the Midwest Shippers Association urge you to change the current blanket exemption policy for these rail shipping categories, particularly as it pertains to the lack of any regulatory oversight of intermodal shipping. And we would like to make some recommendations for starting out and establishing what we hope will be fair, reasonable oversight and regulatory procedures that will provide for reliable, cost competitive containerized rail shipping from the Upper Midwest and inland areas to the ports and world markets. I can tell you that failure to do this could seriously jeopardize the future export business of a wide range of agriculture and grain trading international businesses in the Upper Midwest and other regions – *if the trends of inland intermodal container shipping of the last few years continue.*

And I can also tell you, if we – railroads, ocean carriers, shippers, and regulatory agencies -- <u>succeed in establishing cost competitive, reliable, dependable inland intermodal container shipping service from more locations along our intermodal rail service lines</u>, *we can achieve tremendous growth and economic benefit for Upper Midwest agriculture, for our transportation shipping providers, and for our Nation in future years.*

About the Midwest Shippers Association --

The Midwest Shippers Association is a regional trade association cooperative made up of producers, processors, international traders and exporters of grain, oilseed and food ingredient products. MSA's membership also includes shipping logistics and grain industry service suppliers to our region, which covers the states of Minnesota, North and South Dakota, Iowa and Wisconsin. MSA promotes opportunities to farmers to grow value-added specialty grains for export. We also promote these premium grains and oilseeds to international markets on behalf of our members. And MSA represents its members and seeks to improve and protect our export shipping means from our region. MSA serves as The Network for this value-added crops industry in the region, and works in cooperation with many other commodity organizations regionally and nationally.

Some of our MSA member companies ship commodity grains to the Pacific Northwest by rail hopper car for transloading into containers for export. This is an important and growing segment of U.S. grain exporting.

However, the core group of MSA member companies handle what are called "identity preserved" (IP) food grade specialty grains and oilseeds. They are grown under contract by their farmer suppliers and must be carefully cleaned, sorted, bagged and shipped by intermodal container direct from the processing plants to their customers oversees. These higher value, food grade products are inherently suited for – in fact demand – shipping by intermodal containers. These containers can be loaded and sealed at the plant, then shipped by truck, rail and ocean vessels direct to their customers throughout the globe.

Midwest Shippers Association was first formed through efforts of the Minnesota Legislature, which foresaw the need for an organization to address the shipping needs of IP grain exporters because it understood that access to cost competitive intermodal container shipping would be crucial for the success of this growing opportunity sector of U.S. agriculture.

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While the advent of intermodal container shipping over the last 30 years provided a great opportunity for this value-added, international trade-oriented sector of agriculture to take hold and grow – what has evolved and over the last few years in the way the railroads and ocean carriers are operating inland container shipping is causing worrisome problems. There are severe cost competitive issues for many shippers in our Upper Midwest region, and for other locations as well.

I want to emphasize that the Midwest Shippers Association fully understands and supports that both the railroads and the ocean carriers need to be profitable enterprises. We depend upon them to deliver our products worldwide, and we know they need to make money -- just as our members businesses must be profitable to continue to provide the valuable service they provide.

We do not believe, however, this should mean extreme profits that come at the expense of shippers and our customers to the extent that it threatens the existence of our supply chain businesses. Moreover, we believe rates and service practices need to be set that are not overly distorted to favor certain geographical areas, while unfairly penalizing others, or threatening the global competitiveness of ag production regions that should logically be highly competitive. Just as the railroads and steamship lines must be profitable, the agricultural businesses they serve must also be profitable.

Well, the railroads by all accounts are doing more than holding their own on the profit picture.

According to stories within the last two weeks in Journal of Commerce (since January 20), the railroads' fourth quarter financial performances were:

-CSX profit rose 42 percent from a year earlier to $430 million. Intermodal traffic grew by 11 percent. Profits for the full past year were up 37 percent to $1.56 billion.

-Union Pacific's net profit jumped 41 percent to $775 million in the fourth quarter. Intermodal traffic up 10 percent.

-Norfolk Southern's profit climbed 31 percent to $402 million. Intermodal traffic was up 13 percent and revenue up 16 percent in the fourth quarter.

- Kansas City Southern's net profit was up 60 percent to $52 million in the fourth quarter comparison. Intermodal traffic rose 24 percent, with revenue up 28 percent.

-Canadian Pacific reported a 27 percent fourth quarter rise in profit to $187 million. Intermodal traffic grew 10.5 percent with corresponding revenue up 9.9 percent.

-Canadian National's 2010 quarter profit grew 18.6 percent from a year earlier to $503 million. For the whole year, CN earned $2.1 billion, up 13.5 percent

-We did not find reported results for Burlington Northern Santa Fe, now a private company. However, we would expect them to follow suit with the other Class 1 railroads.

Intermodal container shipping is a complex industry. Solutions to problems do not come easily. Both the railroads and the ocean carriers have equal, interdependent roles in determining the actual costs, service available, equipment availability and rates charged to shippers at inland locations.

One thing shippers have learned – anytime there is a problem... or question about rates, or access to containers, or delivery service – the railroads and ocean carriers, are quick to point the finger at the other party as the culprit or barrier to a reasonable solution.

Whereas in the beginning, the railroads developed many inland rail yards to handle containers, over the years the railroads began to abandon container service at more and more intermodal yards. Today, when it comes to inland intermodal, the Class 1 railroads have geared their business model to "hook-and-haul", as fast as possible, to and from the 9 million+ population Chicago metropolitan area, and the Toronto market in southern Ontario, Canada. Stopping anywhere else is treated like an unnecessary bother to be dissuaded. That means dissuaded through higher rates, and limited or curtailed service.

For example, only a few years ago, BNSF operated a small intermodal facility at its rail yard in the Fargo-Moorhead area at Dilworth, MN. That yard, I've been told, handled 20,000+ lifts at one time not long ago. For whatever reason, the decision-makers determined that the facility didn't serve their purposes as well as they would like. Rates were raised for container shipping from the Dilworth facility to the point that local ag export shippers – (and there are many in this prime growing area for a variety of specialty grains and crops) – found that despite the high cost, it was cheaper to arrange to dray containers from the Twin Cities to their facilities for loading, then back to the St. Paul BNSF yard, where the box would be put on a rail car and hauled right back through Dilworth, often within 50 miles of the shippers.

The Twin Cities Minneapolis-St. Paul 3- to 4- million population area is served by two intermodal rail yards – a BNSF yard in St. Paul and a CP rail intermodal yard in Minneapolis. These important, but undersized, Twin Cities container yards serve a large exporting region including all of Minnesota, much of North Dakota (until recently virtually all of North Dakota), South Dakota, western Wisconsin and northern Iowa.

Equipment Shortages -- Yet as important as this region is for exporting ag products to world markets, the Twin Cities frequently experiences shortages of equipment during various times of the year. While the most current situation has seen adequate supplies of equipment, throughout much of last year and in previous years we experienced shortages of containers. Sometimes desperately so. In general, the Twin Cities is known to be an equipment short area much of the year.

The great irony is, the major BNSF intermodal main line trains roll right through Twin Cities – delivering imports to Chicago from the Pacific Northwest ports and heading back on the return. The recent Minnesota Department of Transportation's State Rail Plan study identified Minnesota as having a huge amount of intermodal rail traffic by its class 1 railroads – yet it is far and away just "pass through" traffic.

Growing Rate Disparities – Perhaps our greatest competitive concern is the growing rate disparities for intermodal shipping costs from the Twin Cities and other Upper Midwest markets, like Omaha, to global markets.... compared to other markets favored by the current system.

The export shipping rates from the Twin Cities to our Asian food and feed markets are far higher than from Chicago, despite the fact that we are the same or closer distance to the ports. In fact, we also have far higher rates than the Toronto area of eastern Canada to Asia, despite the even greater distance.

Last August, one MSA member exporter polled several freight forwarders his company uses to compare rates for shipping from the Twin Cities, Chicago and Toronto to three Asian ports. The lowest rate they found for Chicago to Yokohama was $1,475. From Toronto to Yokohama was $1,695. From Montreal, way on the east end of North America, to Yokohama was $1,775. From Minneapolis to Yokohama, the best rate found was $2,420. That was nearly $950 more per box to ship from Minneapolis to Japan, a closer distance, than from Chicago to Japan...and several hundred dollars more than our competing region of southern Ontario and Quebec, which is much further from the destination.

Those rates, at that particular time, likely reflected spot rates due to a larger flux of imports starting to come into Chicago for retailers stocking up for the Holiday season later.

But still, these rate disparities seem to keep growing. And at some levels, they go beyond rational sense.

Export shippers in our region often have faced major competitive disadvantages because it would cost roughly $300 to $600 more per box to ship from the Twin Cities yards to Asian markets compared to Chicago (the higher number if they had a longer trucking dray from eastern North Dakota/western Minnesota to the yards, compared to closer local shippers). Now, those rate disparities seem to keep ratcheting up ever higher, and are posing a threat to our industry.

There is also a growing concern by Midwest area shippers that more ocean carriers will eventually stop their inland container service and simply go to water-to-water moves – particularly after the wider Panama Canal opens in 2014. The ocean carriers simply may be tired of dealing with the large, uncompetitive Class 1 railroads that control inland intermodal service.

Service Concerns – BNSF in recent years has developed a large, efficient intermodal yard outside of Chicago at Logistics Park. It is a model for high volume service for inland rail coming in from the Pacific Northwest, and the Southern California Ports and other locations. We commend BNSF for developing this. However, some MSA shippers have been advised that most, if not all, of the intermodal shuttle trains coming out of Logistics Park heading to the PNW don't even stop at the St. Paul BNSF yard. They slow down, but keep rolling...stopping only in Minot, half way to Seattle for refueling and crew change.

The Twin Cities yards, and other yards in the region like those in Omaha/Council Bluffs, need to have more dependable, cost competitive container rail service. Moreover, there needs to be reasonable repositioning rates for moving containers from areas of surplus container supply when they are short in our export-oriented markets.

One positive recent development is an effort by BNSF to support a community-developed and funded intermodal yard in Minot, N.D. While that location is suited to serve export shippers in central and western North Dakota, and eastern Montana, the yard seeks to serve a broader area including all of North Dakota. But to date, the costs and rates of service have been prohibitive for the larger volume of shippers on the east side of the state to be able to use the facility. We are hopeful the rates to and from the Minot yard can reflect what logically should be lower rates to and from the PNW ports for much shorter distances with two-way traffic. This yard operated by North Dakota Port Services has recently found substantial current and increasing future import demand for containers hauling in "frac sand" to serve the nearby oil fields. What should be lower rates, can drive the success of this new project and thereby widen its service area. If the rates don't reflect those shorter rail distances and two-way hauls, then it will be a challenge to develop sustainable business.

As for the Twin Cities, shippers are concerned that the St. Paul yard could eventually run a similar fate of the Dilworth yard – priced out of being able to offer competitive shipping.

The question should be asked – when the rate differences are so wide, and so much in favor of Chicago compared to nearly all the other significant inland metropolitan areas – the Twin Cities, Denver, Omaha, Salt Lake – is it any wonder why all of the major retail changes put up their new distribution centers in the Chicago area?

Once the competitive economics ball starts rolling downhill in that direction, it is only logical that they will locate there. And the result is more and more goods are having to be trucked longer distances, at greater cost and less efficiency.

Velocity is frequently cited as a reason why the railroads just don't want to stop between Chicago and the ports. Get the trains rolling, you don't want to slow them down or stop.

But our grain export shippers also value velocity. We just feel velocity and service need to be considered from where the freight originates and goes to the end destination. It should not be only a matter of railroad velocity. When a shipper needs to truck his or her freight 300, 400 or 500 miles in the other direction from the destination port, to put it on an intermodal train that runs right back through his area or state..... how does that train's velocity serve the overall purpose?

Yet exporters, like our members -- who face tight price competition with other countries -- are increasingly losing sales – purely due to competitive shipping costs or lack of timely rail service. Lately, it extends beyond intermodal service to include problems with hopper care and box car availability and costs.

Our members who export identity preserved specialty grains also advise that there is growing demand by their customers in Asia for "just in time service". Just as the major U.S. retail importers are gearing their supply chain systems for just in time service and planned, carefully timed deliveries from the original point of manufacture, our food manufacturer customers overseas also increasingly want to have that kind of supply relationship with their food ingredient suppliers here in the U.S.

"Uninterrupted, consistent and competitive service is critical to serving the large consuming populations, particularly in southeast Asia, " one experienced MSA member exporter advises. The intermodal system is designed and intended to provide just that service.

Among MSA members, more than one company has indicated that they believe they could develop the export sales demand, and the farmer producer suppliers, to enable them to expand their businesses and hire more workers – but they do not have the confidence that they will have reliable container shipping service at competitive rates that enable them to take on that investment risk.

Intermodal container shipping is an absolutely critical factor for America's export competitiveness. If we are not using it as it is capable of being used to serve our exports, then we are figuratively and literally missing the boat.

Certainly ocean carrier rates and services for inland shippers are a critical factor. But railroad intermodal rates and service practices are a key underlying factor in overall export shipping costs and therefore, for the outlook for value-added agriculture exports -- whether it's for dry containers for value-added grains, or refers for meat, poultry and dairy exports.

Recommendations –

We urge the Surface Transportation Board to take steps to change the current blanket exemption from any regulation of intermodal rail service, and to establish reasonable oversight practices and procedures that will lead the rail intermodal industry to adopt fairer, more appropriate rates and services to serve Americas exporters and importers.

- **Reporting Requirements**

It is time to lift the veil that the industry maintains over its real intermodal rates and service practices. Enabled by the current STB exemptions, the railroads -we are told -mandate strict confidentiality regarding their rates and service contract provisions with the ocean carriers. <u>It is high time that more transparency be required of this important transportation sector.</u>

We have been advised that there are often incentives and disincentives built into rates that lead ocean carriers to move boxes back to the original ports, often as empties, rather than to allow them to be repositioned to other locations where there may be demand for an export load.

The truth about these practices is hard for us shippers to know. But the practices, which affect our ability to move equipment where needed, should be examined in detail to understand their impact and to determine if changes need to be made for the good of our export transportation needs.

The STB should adopt reporting requirements and procedures for rail intermodal service contracts with ocean carriers to provide more transparency over rail service and rates -- for different locations, for repositioning, for moving empties and loaded containers.

If that specific reporting information needs to be kept confidential from shippers or carriers for some reason, the STB should develop a procedure for communicating to the public the parameters and practices on a regular basis.

The truth in these intermodal practices is a difficult animal to find because of all these strict confidentiality requirements. Reporting and increased transparency is needed to find out what is really going on. That is the place to start.

- **Reasonable Repositioning Rates**

We need the Class 1 railroads to provide less costly ways to move containers from surplus areas of the country to where they are needed when equipment is in short supply. Reasonable repositioning rates by the railroads are needed to be able to make the intermodal system work as intended.

The intermodal system is wisely geared toward two-way moves, rather than the one-way hauls typical of other rail car moves. But not all return loads can be expected to be located right near the heavy import markets. Some repositioning should be naturally expected, not considered a wild idea to be avoided in their standard operating practices.

We can have much more success achieving our export expansion goals if we are able to make the intermodal container system better serve our exporters where they are located. Leaving incentives and penalties in place that lead carriers to send more boxes back empty will not help us reach our export goals. There is a cost to reposition equipment to be sure, but the more reasonable those charges are to move empties to where they are needed, the better our system will work for moving freight overall.

- **Rates Should Bear More Relationship to Distances and Costs**

Certainly there are operational cost advantages for two-way hauls and moving larger volume trains to and from major metropolitan areas. But the cost rate structures that now favor certain areas, often located much further distances from the ports, would seem to be arbitrary and beyond what is reasonable. There needs to be a closer relationship of rail rates and container shipping rates with actual distances from origination to destination ports. Growing rate differentials are skewering the system.

- **Common Carrier Obligations for Intermodal Rail Service?**

Under the current system of allowing exemptions from any regulation of intermodal rail shipping, it may seem a huge leap to consider common carrier obligations for intermodal for Class 1 railroads. But we think there can be established some reasonable, achievable policies to see that some minimum levels of service and appropriate rates be provided along the main intermodal rail lines in the states they cross. Certainly, not every rail line is going to be able to provide intermodal service. And certainly not every intermodal train needs to be required to stop at all rail yards along the main intermodal yards between Chicago and the West Coast. But schedules could be developed to provide a level of needed service and see that equipment is provided at more locations along the way. The inland intermodal rail system needs to serve more than just the high velocity, non-stop trains.

- **Maximize Short Line Railroads' Ability to Contribute**

There are a number of examples where short line railroads are playing a significant role in handling intermodal container rail service. Examples include a model effort by the Twin Cities and Western Railroad here in Minnesota, and the Iowa Interstate Railroad operating the rail yard in Council Bluffs for Union Pacific and moving containers across the state. Looking to the longer term future, we believe it is important that the U.S. fully utilize the capabilities of short line railroads to contribute to a fast, efficient, wider-serving intermodal rail system.

There should be no allowing of Class 1 railroads to put constraints on short line railroads from providing container service through any past contracts. Indeed, the hub-and-spoke concept for rail service is important to be able to assemble larger volume train service for efficiency. Short lines can contribute to helping cue up larger capacity trains for the Class 1's to haul, and can perform a range of contributing operations.

Conclusion --

Our premium grain and soybean producers, processors and export traders in the Upper Midwest can compete on quality with any other location in the world. Our export customers in Asia highly value our products and the relationship we have with them as suppliers. But we are dependent upon an intermodal container shipping system that currently discriminates against our region on rates and often on equipment supply to an increasing degree. We are often uncompetitive now due to shipping costs – even though we are located closer to the end destination and intermodal trains roll right through our region from further east. If these trends continue, there is a danger to the sustainability of our premium food grade soybean and specialty grains industry in the Upper Midwest region.

We at MSA believe the intermodal container shipping system needs to work for all partners in the system. It needs to work for the shippers too.